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# After the End of Transition: Policies for the New Innovative Entrepreneurs in Bulgarian Economy

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## SUMMARY

The paper argues the need of public policy in support of the innovative entrepreneurship in Bulgaria. This issue receives special importance in the context of final stage of country's integration to EU and expected membership in 2007. In 2000 the European Council has defined in Lisbon its objectives for 2010 the Union "to become the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion". It stated that a friendly environment for starting and developing businesses is central to reaching these goals. The importance of entrepreneurship has been reaffirmed in the EU Commission's 2003 Spring Report to the Spring European Council, and later has been developed into policy strategy in the *Green Paper Entrepreneurship in Europe*, adopted by European Commission in January 2003. In particular, the *Green Paper* outlines four key contributions of entrepreneurship:

- *Entrepreneurship contributes to job creation and growth, and it fosters social and economic cohesion for regions whose development is lagging behind;*
- *Entrepreneurship is crucial to competitiveness*
- *Entrepreneurship unlocks personal potential*
- *Entrepreneurship answers societal interests, providing societies with wealth and diversity of choice for consumers; it plays a positive role in delivering health, education and welfare services efficiently.*

Bulgaria has passed through the one of the most difficult and painful transition from administrative socialist economy to the market economy. For almost a decade in the country has been established a specific kind of rent-seeking and assets-scraping capitalism imposed by political nomenclature of former Communist party. It eroded the industrial and knowledge base, undermined the initial enthusiasm and entrepreneurial spirit of people, and prevented country's rapid integration in global economy by consciously imposing barriers to the foreign direct investment. The real reforms in the country started only in 1997 and it was not until the last several years when Bulgaria reversed the negative trend of its economic development making steady progress towards integration in Europe Union.

The paper argues that in current situation encouraging entrepreneurship and providing better economic and institutional environment for the existing innovative SME is one of the most effective ways to boost economic development, create employment opportunities and improve competitiveness of Bulgarian economy. It is based on empirical study of the *innovative small and medium private firms* in the sectors of *Innovation & Communication Technologies* and *Perfumery & Cosmetics*. The findings make possible to outline key problems of the innovative entrepreneurs as *potential bearer of 'technological renaissance' in the country*, to define the objectives of relevant public policy and propose policy actions in the field.

The present paper include the following proposals:

- Launching special campaign in public media promoting entrepreneurship;
- Advancing development of venture capital in the country;

- Strengthening research and education infrastructure in the regions, where the clusters of innovative SME in specific sectors have been established;
- Support of local administration in developing capacities to assist development of innovative entrepreneurs
- Improving institutional capacities and human potential of branch associations of entrepreneurs and inducing changes in their strategies;
- Initiating (or providing support where it exists) collaboration between branch associations in given sector or between those in related sectors
- Empowerment of entrepreneurs' Branch associations by transferring to them some of the government responsibilities in steering economic development in the sectors

## BACKGROUND

This section intends to shake some of the well-established views about economic transition in Bulgaria by adopting entrepreneurial viewpoint on the events that took place during last fifteen years. It argues that unlike Central-European countries, the 'velvet revolution' in Bulgaria was actually used by specific wing in Communist party nomenclature to transform its political power into economic one. This wing preserved control over practically all sphere of Bulgarian society until the late 1990s. One of the main features of this period was the suppression of the initiative and entrepreneurial spirit of people, explicit attack against independent entrepreneurs and imposition of a negative public image of entrepreneurs.

During the post-socialist transition the innovative entrepreneurs in Bulgaria have been working in hostile economic and political environment of rent-seeking and assets-scraping capitalism. This specific form of capitalism originated from the events that took place in the last decade of socialism. It was marked with intensification of the struggle between two main wings of communist nomenclature – “political” and “economic” ones.<sup>1</sup> The *political nomenclature* comprised the members of organizational and ideological departments of communist party together with special services as their ‘right hand’ (including those monitoring foreign trade with the West). It possessed the main asset (or ‘capital’) for steering every field of society – *control over the ‘cadres’*, the appointment and promotion of relevant people on key positions. With the reforms that have been gradually introduced in Bulgaria since late 1970s the dominant positions of political nomenclature have been challenged by the increasing power of *economic nomenclature*, i.e. the ‘cadres’ managing the economy - from the lowest position of directors of the enterprises, through the managers of the large vertically integrated state ‘combines’, to the heads of economic ministries and their officers. The later has developed its own sense of unity, its own ‘industrial ethos’ and managed to establish itself as a group opposed to the political nomenclature. From this point of view *the history of the higher echelon of Bulgarian Communist Party was marked by several big clashes between these two wings, each time the political nomenclature taking over the economic one*. This happened first at the end of 1960s with the dismantling of legendary economic cartel “Bulgarian Sea Fleet” (former TEXIM), when the founder and chief manager of the cartel Georgy Naydenov was prosecuted and put in jail under false accusations. The same happened in early 1975, when Prof. Ivan Popov – the man who initiated the successful

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<sup>1</sup> More on internal tensions of communist nomenclature see in: Boundjulov, A. 2003. ‘What Emerges in the Place Of? Artificial Joints and Networks Under Socialism’. In: *Historical sociology of socialism: special issue, Sociological Problems* 1/2 (in Bulgarian).

development of electronic industry and later became deputy Prime Minister and member of Politburo – was dismissed from all his positions and send ambassador to Switzerland. Their high recognition in Bulgarian society, especially among industrial managers, threatened the power of party's organizational and ideological departments, including top leadership of the country.

However, the economic nomenclature recovered soon and by early 1980s it managed to create a special organizational structure, the Bulgarian Industrial Economic Association (BISA), which copied the structure of Japanese federation of industrial branch organizations.<sup>2</sup> BISA became very popular with its initiatives aimed at optimizing the economic development. It backed the attempts to relax administrative control, to allow small-scale private property in industry and agriculture, to enforce foreign economic relationships with Western corporations, etc. Remarkably one of these initiatives was to boost the development of small and medium enterprises and to endorse them with bigger autonomy in comparison with other socialist economic organizations. Some these SME resembled Western spin-off firms – they have been build on indigenous innovations or used licensed Western technologies.<sup>3</sup>

On the eve of the radical changes in November 1989s, the economic nomenclature was defeated again. In December 1988 Ognyan Doinov – the most popular economic leader in the country and highly respected among Bulgaria's Western economic partners - was dismissed as member of Politburo. Similarly to the cases of Georgy Naydenov and Ivan Popov, his removal was a sign the same to be done with his followers in economy, state and party apparatuses. The economic power was taken again by political nomenclature.

*So unlike Hungary, it was the political nomenclature – whose representatives in his vast majority considered the economy through the optics of old Marxist political economy and lacked specific industrial managerial skills – which was destined to carry out post-socialist economic transformation in Bulgaria.*

Instead of opening door to the foreign investors, to empower the most talented industrial managers and to promote entrepreneurial spirit among the economically active population, which for more than 50 yeast have been deprived from the very conditions to became entrepreneurs (property rights and fair access to credit), the representatives of political nomenclature did just the opposite. Seeking to preserve their dominance in society the 'reformers' adopted a *strategy of conversing their political capital into economic one*. They successfully used the conservative neoclassical models the Western economic experts were selling after 1989 to push out the economic nomenclature from the positions it still possessed and to impose their own rent-seeking and assets-scraping strategies. These strategies included number of interrelated measures, the most important of them were:

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<sup>2</sup> This time the industrial managers were headed by an younger, but equally influential member of Politburo – Ognyan Doinov, who in late 1960s has spent five years in Japan as manager of very successful Bulgarian-Japan joint venture. In his memoirs Doinov wrote that BISA was established as conscious attempt to help "the true" industrial managers, which he considered as "the most underprivileged part of nomenclature, being under constant pressure of administrative system but nevertheless attempting to do their job professionally". These people, he wrote, have been dispersed in their posts with no colleagues help, no consultancy available and no possibility to voice their opinion and defend themselves at the local and regional party authorities."

<sup>3</sup> Special ordinance limited their activities to light industry only. The political nomenclature feared that these new forms of economic activity contained "too much capitalism".

- 1) Gaining control over country's financial system by appointed trusted people at now independent bank system (special amendment of law stipulated that bankers are not personally responsible for the loans they allowed!);
- 2) Keeping large share of state property in industry, while dismantling former vertically integrated structures (state combines) and establishing stringent control over the industrial managers of separate enterprises (via bank system, by appointing trusted people, by means of specially created criminal groups, etc.).
- 3) Exploitation of the state-owned plants by the schemes of so-called "input-output economics", i.e. compelling their managers to buy raw materials at higher price from specific supplier and to sell their production at lower price to specific distributor (usually both small trade firms, privately owned by the representatives of political nomenclature working in given sector).
- 4) Not allowing penetration of foreign capital for as long as possible;
- 5) Suppressing the emerging independent entrepreneurs from other social groups by limiting their access to credit and forcefully pushing them out of the most profitable sectors;
- 6) Control over legal system by appointment of trusted people and by introducing special legislation with cut off the legal system from public control and accountability.

The process of restitution, launched in 1992 that returned the property nationalized in 1947 to the former owners was slow, incomplete, and was successfully used as ideological coverage of the real economic processes that were taking place. Worst at all, *the restitution mentality promoted by this process was practically identical with economic philosophy of political nomenclature*. It also implied rent-seeking capitalism, focusing public attention on the possession of property (most of which were outdated material assets) instead on the opportunities for making money by new ventures and on related emancipation of credit system from the political system by creating conditions for fair access to credit. Preserving its control over the new 'independent' public media, the ruling elite consciously discredited the emerging patterns of entrepreneurial activity. They continued to spread an atmosphere of distrust to private initiative and its leveling to a type of semi-criminal activity. There were fewer examples of successful entrepreneurs that managed to creep into the media.

Hence the new Bulgarian state and political institutions have emerged after 1989 as something very different in its nature and functions from its Western analogues. They have not been based on principles of accountability, civil service, clear identification of policy objectives and the related public interests. Rather, Bulgarian political system was used by the winners in the battle between two wings of communist nomenclature as a shield that guaranteed the flawless application of their rent-seeking and assets-scraping strategies to gain economic superiority.<sup>4</sup>

The results of this type of economics were hundreds of 'sucked out' state-owned firms – highly indebted, with outdated and badly maintained equipment, paying meager salaries, and left out by their best workers and specialists. Combined with grain shortages and high inflation, this has led to the mass upheaval in the winter of 1997, preliminary elections and

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<sup>4</sup> That is why the 'bandit model' of Mansur Olson on the governments' role in East European economic transformation provides appropriate framework for conceptualizing situation – the model defines the role of politicians and bureaucracies in post-socialist economies as 'bandits' attempting to extract maximum resources from the 'public' and introduces relevant variables such as the ability of the 'public' to resist, the time span of bandits' economic policy and the level of bandits' internal cohesion. (Olson 1995: 437-462).

new democratic government. The new government in few months has closed 16 ‘drained’ private banks, introduced currency board and launched rapid privatization program. Three years later the share of state ownership in the economy fell from over 70% to below 30%. The complete domination of ex-communist political nomenclature was finally broken. For few years, however, it was replaced by fairly similar in its effect ‘democratic domination’, where the democratic government exercised strict control over the privatization process and economy as whole, favoring its own party apparatus. Paradoxically enough, by 2001 it became clear that state and political institutions have been used again for the enrichment of another politically bound group.

According to the latest surveys among business circles, it was not until the government of ex-monarch Simeon SaxCoburg-Gotha came to power in 2001 that the state institutions adopted relatively neutral attitudes towards the private companies independently of their belonging to the groups of former ex-communist or ex-democratic nomenclature, or to those of independent entrepreneurs.

The invitation of Bulgaria to become member of EU in 1998 and the ongoing negotiations with EC have been another important source of changes in Bulgarian post-socialist political system towards Western standards of behavior, including the changes in relationships between political and economic spheres.

#### CURRENT SITUATION

The results of our research have shown that ‘conversion’ strategy of political nomenclature did not succeed in full scale. There were sectors, which provided sufficient enough conditions for the innovative entrepreneurship to emerge, develop and grow. Their representatives came from different background – R&D centers in industry, industrial managers fired off by the political nomenclature in the years before and after 1989, ancestors of former capitalist class that restituted their property, or simply talented people with entrepreneurial spirit which seized the opportunity for business in the new economic conditions, where the private property was nevertheless legally admitted.<sup>5</sup> Being relatively invisible during the first years of transition and passing through the many hardships, these entrepreneurs gradually increased their economic strength. By uniting their efforts in newly emerging *branch associations*, at the end of the decade they began to exert pressure on the political system to change the dominant model of rent-seeking capitalism.

The result of all these developments is that in 2003 we see Bulgarian economy in rather unstable equilibrium between two main group of economic agents – the *innovative entrepreneurs*, on the one hand, and *rent-seeking capitalists related with former political nomenclature* together with *part of restitution capital* on the other. To these we have to add the *third group* of steady increasing *foreign companies* in Bulgaria, majority of which take the side of innovative entrepreneurs.

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<sup>5</sup> It’s worth to remind the definition from 2003 *Green Paper on Entrepreneurship in Europe*: “Entrepreneurship is first and foremost a mindset. It covers an individual’s motivation and capacity, independently or within an organization, to identify an opportunity and to pursue it in order to produce new value or economic success. It takes creativity or innovation to enter and compete in an existing market, to change or even to create a new market. To turn a business idea into success requires the ability to blend creativity or innovation with sound management and to adapt a business to optimize its development during all phases of its life cycle. This goes beyond daily management: it concerns a business’ ambitions and strategy.” (page 5)

We could tentatively define *two complimentary principles*, which taken together help differentiate the sectors ‘conquered’ by the representatives of post-communist political nomenclature from those where the innovative entrepreneurs have better chance to develop.

The first principle is the overall *profitability of the sector*. The political nomenclature as defined above, focused on most lucrative sectors such as production of mass consumer goods for domestic market (tobacco, alcoholic beverages including wine, petrol derivatives, pharmaceutical products, cosmetics and household chemistry, etc.) or trade that deliver such goods (especially import), as well as sectors that still have competitive advantages at the international markets – ferrous metals, wood and wood processing industry, heavy chemistry, electric power industry, etc. We should add to this group service sectors such as telecommunications and tourism, although their specific characteristics brought about some long term constraints for pure rent-seeking strategies. Only few very strong multinational companies have been able to limit in certain extent the power of political nomenclature in these sectors, often with the help of Western governments and after paying serious concessions. However, the *low-profit sectors* - those producing manufactured goods or provide services with relatively limited demand; those having low prospects for export; those requiring significant investments and expensive maintenance, those with long return cycle of profit, etc. – remained relatively free for entrepreneurial initiative.

The second principle is *the sectors inherent resistance* (or better ‘rigidity’) *to the rent-seeking and rent-scraping strategies*. Political nomenclature might also be considered as a newcomer and from this point of view we could distinguish between *sectors with ‘low entrance’* and *‘high entrance’ barriers*. The former did not require specialized know-how or they implied know-how similar in kind to that possessed by the representatives of political nomenclature (for example trade with consumer goods and petrol derivatives). In these sectors its representatives have easily taken command positions and have been able effectively to manage their new business. The traditional industries of mass production like ferrous metal, heavy chemical industry, etc. should also be included in this group, because here the ability to control of low-skilled employees (both in production and in system of distribution) was key asset, and it was relatively easy to sustain mass production at acceptable quality. Usually here the output consisted of low-tech products, which did not require special maintenance, nor developing special services to customers. In addition to that, in these sectors breaking the existing regulations, industrial standards, intellectual property rights, etc. was not punished because of submissive government institutions and hidden control of legal system.

However, there were also sectors with *high entrance barriers* - where the very production process and specificity of the products presupposed specialized knowledge hence they used skilled labor and management; where the maintenance of the products and trust between producer and his customers (or between service provider and his clients) was crucial for the business. In majority of such cases it was difficult for the political nomenclature to develop sustainable business – for example in IT industry the most successful business of its representatives was to re-sell abroad the sophisticated equipment of electronics plants, imported previously with utmost efforts through the Western embargo...

The comparative study of the two sectors of *information & communication technologies (ICT)* and *perfumery & cosmetics (P&C)* lead us to the following main points, outlining current situation:

- 1) For the last 14 years of transition in spite of hostile economic and political environment in the country there emerged substantial number of vital and fast



- developing private innovative SME, whose seek to impose their own agenda to the political system, and to make it better responding to their specific needs and interests.
- 2) Development of innovative SME in these sectors has reached a stage of differentiation and specialization. There even emerged high-tech firms that specialize in providing innovation and engineering services to the other firms and for export.
  - 3) There is clear regionalization of certain types of businesses. Innovative SME in given sector often emerge as clusters in certain regions because of specific tradition (for example large enterprises from the socialist period), presence of relevant research and education infrastructure, local cultural or natural environment, etc.
  - 4) The large majority of studied innovative SME demonstrate socially responsible behavior towards their employees and local communities; they are correct towards their business and financial partners.
  - 5) The attitudes of local authorities and government offices towards innovative entrepreneurs vary from real collaboration and partnership to hostility, creating barriers to their development and insolent corruption.
  - 6) During the years of post-socialist transition the innovative SME have been working in changing conditions at the internal and international markets, unpredictable financial and legal environment, unstable political process. At their markets the firms compete with Western firms and the firms of other post-socialist countries.<sup>6</sup> Often their competitors receive direct or indirect support from their governments, such as export subsidies, protective import taxes, and subsidies in hiring employees. There is no such backing on the side of Bulgarian government.
  - 7) Working without assistance of government institutions (the later often being source of additional troubles), the innovative entrepreneurs managed to cope with various obstacles transforming their failures into source of experience and points of support for the next move ahead. They develop abilities to analyze and learn from their experience and invest continuously in new technologies, design of new products and services, in qualification of their employees. They are very flexible, often diversify their activities and enter new markets.
  - 8) Their business ethics deserves special admiration, because although developed in the hostile conditions of Bulgarian rent-seeking capitalism of 1990s, it reproduces the classical entrepreneurial spirit of vigor, persistence, the hard work trust and correctness towards the customers and business partners, etc.<sup>7</sup> We have found in number of firms the children of entrepreneurs studying the same specialty at university with clear intention to continue one day the business of their parents.
  - 9) The innovative entrepreneurs have developed habits not to rely on government and political institutions in the business; they prefer not to enter in dialogue with these institutions. However, this reduced their ability to define their problems and to frame them in appropriate way, lead to the lack of skill for lobbying, etc. This might turn to be counter-productive at the present period of negotiation between government and

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<sup>6</sup> For example Bulgarian cosmetics firms compete with big world producers at local market and at the same time they compete with them and with local firms at Russian market of perfumery and cosmetics. Bulgarian and Romanian software firms compete at Western market of software

<sup>7</sup> The experience of innovative entrepreneurs sharply differs from those of representatives of rent-seeking capitalism, which heavily relied on political and state backing of their activities and on financial and legal 'comfort' they provide – possibilities not to repay their credits, to delay social and health securities, to pay reduced taxes and custom duties, to break intellectual property rights, etc. That is why changes in political power often lead to bankruptcy among the "party" firms.

European Commission about economic and other conditions of EU membership. Here the collaboration with between entrepreneurs and government is highly needed.

- 10) The majority of innovative SME realize the necessity of collective actions in defending their interests and those of the sector as whole. They are organized in branch associations, which try to impose the rules of business ethics and to elaborate collective positions towards those who violate these rules. The branch associations have developed number of activities supporting the business of their members – such as transfer of experience from developed countries, training in introducing good management practices, establishing contacts with political parties and government institutions.
- 11) The expansion of the activities and responsibilities of branch associations poses serious challenges to their development – they often lack enough resources, there are difficulties in hiring qualified staff, etc. These and other difficulties might result in serious crises in their development.
- 12) The innovative SME have specific needs and face different problems, which vary not only between sectors, but also inside the sectors. This makes the dialogue with government and political institutions rather difficult. The traditional arrogance of state officials towards private businessmen<sup>8</sup> is another obstacle. They are not inclined to listen to the entrepreneurs and often are offering standard and general solutions, having little in common with concrete problems of firms. Key positions in government offices are held by people without qualification and which are unable to understand the problems of entrepreneurs. Frequent staff changes in these offices because of political and other reasons are another barrier to collaboration.
- 13) Coming EU membership will bring substantial changes in the businesses in every sector of the economy. This is a major challenge to the entrepreneurs and they make serious efforts (alone or in the framework of their branch associations) to be informed about EU specific legislation, standards and norms that refer to their products and services. They invest serious resources to meet these requirements by introducing new technologies, systems for quality and good management practices. However, they are univocally assert that government officials carrying out negotiations with EU *do not inform the business, do not talk with entrepreneurs and rarely ask for their opinion.*

## OBJECTIVES

The objectives of the policy in support of innovative entrepreneurs in Bulgaria are:

- 1) To induce changes in overall public attitudes towards innovative entrepreneurship in the country;
- 2) To strengthen the potential of innovative SME in different sectors by targeting several key problems of their development – knowledge base, institutional capacity of their branch associations; patterns of business partnership;
- 3) To change relationships between political & government institutions and branch associations of entrepreneurs, which have been established during the last decade and which do not correspond to current economic changes at the eve of EU membership.

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<sup>8</sup> This is a tradition, which roots go deep in Bulgarian past, far beyond the communist period – to the times of state capitalism during the first half of the last century.

## KEY ISSUES

If continue, the current lack of appropriate policy supporting innovative entrepreneurship in the country would deepen the existing and give rise to new problems. The following issues are to emerge, hindering the prospects for growth:

- *Scarcity of well-qualified technical staff, university graduates and R&D specialists.* The crisis in country's higher and university education, caused by the persistent underpayment of the teaching staff and lack of investment in material base, coupled with never ending brain drain of best professors and students are eroding the human resources needed by innovative SME to sustain their high rates of growth.<sup>9</sup> With the aging of top R&D specialists trained in R&D centers of former state corporations (combines) a generation gap appeared, which is very difficult to be filled in. There are fewer doctoral students, and in-house training requires years of apprenticing.
- *Continuous degradation of research and knowledge base of innovative entrepreneurship, especially at regional level.* Like in other sectors, the newly established innovative SME in the field of ICT and P&C have benefited from the scientific and R&D infrastructure inherited from socialist period. Many of successful entrepreneurs in these sectors came from R&D centers. However, with the closing of these centers and narrowing the scope of R&D activities in the new private firms, some important areas of fundamental and applied research simply vanished. Traditional fields like ion implantation in semiconductors or synthesis of new active substances for cosmetic industry practically do not exist anymore. This will erode the prospects for growth of innovative firms and will reduce their long-term competitiveness.
- *Lack of long-term planning at firm level and lack of sectoral developmental strategies.* The innovative firms' limited resources and their preoccupation with immediate problems shorten the scope of their business projects. However, number of leading innovative SME have already reached a stage where the long-term strategic planning is vital necessity. The insufficient investments in this area, the limited use of consultancy services and feeble collaboration with universities and other research establishments deepen the problem and makes innovative SME vulnerable to the market shifts.<sup>10</sup>
- *Growing tensions inside branch associations.* Most of these associations have emerged as unions of innovative private SME in order to resist better to the hostile behavior of large state-owned firms, controlled by ex-socialist political nomenclature and 'bandings' from the government. During the last several years with government taking equal stand to various business groups, the external threats diminished. On the other hand, there

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<sup>9</sup> In certain segments of ICT sector like software the firms are sending some of their top specialists to teach at corresponding university specialties in order to reduce costs for individual training of poorly qualified graduates.

<sup>10</sup> According to the word of an university professor and top R&D expert in P&C sector: "...Most of Bulgarian cosmetics firms are used to rely on the ingredients and standard formulae provided by the big multinational suppliers. Hence they are lagging behind the leading companies - there are fewer original products developed, even less brand series. Then how can they go through on the European market? It is only the Russian market where they are still selling well, but sudden changes like 10% increase of custom duties last year make the firms extremely vulnerable. This is because they are targeting lower price categories and are unable to satisfy clients at higher price categories. The firms are using high quality ingredients, they have good production technologies, qualified staff and yet they are selling low price products! This is such a paradox. I think the reason is the lack of long-term vision. I am pleading our firms: please establish your strategic departments, set your 3 to 5 years objectives, create something really new aiming and fight to impose it on the market!"

appeared serious differentiation among the firms themselves. In P&C sector there are about ten big firms (both former big state firms being privatized and some of the former high growth SME), 30 to 50 well developing medium firms and more than a hundred small firms. Besides their common interests, these firms now obviously face different problems and challenges. This makes extremely difficult the elaboration of a common strategy, creates problems and even potential crisis of branch associations.

- *Closely related with the last issue is the difficult emergence of new large Bulgarian companies with potential to become economic actor at regional and even European scale. The coming mergers between larger and smaller Bulgarian firms in various sectors will require substantial restructuring of will shake the existing patterns of relationships both between the business partners and between firms and public institutions. If not faced by relevant public policy, this issue is burdened with serious potential conflicts.*

## ASSESSMENT OF ALTERNATIVES

Not adopting the proposed public policy equals to missing the window of opportunity to rapidly adapt the most promising industrial sectors to the requirements of EU market and to provide condition for sharp economic growth in the country. In particular

- Degradation of knowledge base in specific sectors will continue. Some key competences will be lost or created anew at much higher cost;
- Business partnership in different sectors might experience serious crises due to the institutional weakness of branch associations and growing tensions between entrepreneurs;
- Key deficiencies in government administration and political expertise will not be cured;
- The majority of population will retain its passive economic behavior of paid labor, awaiting someone 'from above' to solve its problems.

## PROPOSED ACTION

*Launching special campaign in public media promoting entrepreneurship.*

The first step in proposed policy is to set a task force of media experts, social and economic researchers on entrepreneurship and representatives of relevant guilds (journalists, video-documentalists, etc.) to design how to make public the daily life of innovative entrepreneurs. The success stories have to be documented, series of articles have to be published in relevant journals, and special TV program should be established at some of the most popular media.

*Further development of venture capital in the country*

Development of fair access to credit for the best entrepreneurial projects is crucial condition for promotion of innovative SME. Venture capital is relatively new and highly efficient form, which combines provision of purchasing power with much needed consultancy in crucial aspect of SME management. It is especially suitable to proposed policy. The already existing institutional forms of venture capital in the country should be given public support and individual initiatives (so called 'business angels') should be encouraged. At present situation it is especially important to focus venture capital in two directions – assistance of larger firms in their efforts to establish themselves on the world market *and* assistance of the emerging innovative SME of new generation entrepreneurs as vital pool for future alternatives for growth.

*Strengthening research and education infrastructure in the regions*

Based on appropriate empirical studies of the established and emerging regional clusters of innovative SME, special measures should be taken for improving the knowledge base of these regions. The simplest way to achieve this goal is Bulgarian Government clearly to declare its adherence to the EU target of setting up 3% share of GNP spending for research and higher learning. Compared with the current less than 0.5%, the doubling of public spending for the next financial year will give clear signal of public support for innovative business and will encourage entrepreneurs also to invest in research and education.

As an additional step the collaboration between business and academia should be encouraged. Measures to fight bureaucracy in research institutions & universities have to be implemented.

*Support of local administration in developing capacities to assist development of entrepreneurs*

The existing program in support of local administration should be complemented with special activities aiming to train local officials to work with branch associations and to better understand the need of entrepreneurs. These measure have to be taken in collaboration with highly efficient NGOs, working in the field and which have gained prestige among local governments (for example *Foundation For Local Government Reform*).

*Improving institutional capacities and human potential of branch associations of entrepreneurs*

Special measure should be taken for training the staff and improving institutional capacities (including their material infrastructure) of branch associations. Policy initiatives shifting the current policies of branch associations should encouraged, by focusing on several key strategic objectives as complimentary to current preoccupation with short and middle term goals. Similar steps are needed in support of collaboration between branch associations in given sector or between those in related sectors

*Empowerment of entrepreneurs' Branch association*

The most important action in improving the role of branch associations is transferring to them some of government responsibilities in steering economic development in the sectors (licensing, control over conformity with standards, elaboration of developmental strategies, qualification programs, etc.). The improved institutional capacities of branch associations are precondition for such actions, but the problems in this area should not be used as justification of excessive government interference in the economy.

**TIMING**

We believe that there is a favorable window of opportunity the proposed action to be carried out and it comprises the remaining two and half years before Bulgaria membership in EU in 2007. This window of opportunity is validated also by the political and financial stabilizations in the country and moderate economic growth during the last several years. It provided condition for the innovative SME in different sectors to stabilize their industrial capacities, human resources and to improve their knowledge base. Taken under these circumstances, the proposed actions will boost their productivity and competitiveness, which eventually will help their survival and growth at European and global market.

## FINANCIAL RESOURCES NEEDED

The proposed policy in support of the innovative entrepreneurship in Bulgaria relies on multiple sources of funding. We consider appropriate for the Government to allocate a limited resources playing the role of ‘seed capital’, encouraging other stakeholders to invest in those actions and measure they consider most suitable for their needs. The best way for allocation of public resources might be in form of specific project under one of EU accession programs – *Phare, Programs for Regional Development*, etc. Branch associations, local governments, Universities and Government research laboratories are among the potential source of funding, not only in money but also in kind.

In such arrangement the key issue becomes coordination of efforts. We believe that such coordination could be carried out by a small *Task Forces on Sector-Specific Innovation Policy Strategies*. The *Task Force* could be the core of project jointly funded by Bulgarian Government and EU accession program. It should be operative for a fixed period of time (three years), with clear measurable objectives and limited staff.

## COMMUNICATIONS

Together with research report, this policy paper will be published as booklet and circulated first among branch associations in the sectors of *information & communication technologies* and *perfumery & cosmetics*. They have been circulated among limited number of experts and entrepreneurs which have had input. At two of branch associations, we have been working with closely, panels are planned to discuss the policy proposal.

Presentations of the present policy ideas have been given in the framework of series of expert meetings “Socialists and entrepreneurs”, organized by political movement “Social democrats” in the spring of 2004. In addition to that, a number of publications are planed in specialized business press. Contacts with relevant government and political experts have been established and they manifested some interest.

Based on his experience, the author expects some of branch associations to become the main engines in promoting the ideas developed in this paper.